

Introduced by Senator Campbell

February 15, 2005

An act to amend Section 53601.7 of the Government Code, relating to local agencies.

LEGISLATIVE COUNSEL'S DIGEST

SB 268, as amended, Campbell. Local government investment.

Existing law, until January 1, 2007, prescribes the instruments in, and criteria by, which a county or a city and county may invest surplus funds.

This bill would additionally specify that up to 25% of the fair market value of the total assets may be invested in the first tier securities of a single issuer for period of up to 3 business days after acquisition and for only one issuer at a time.

Vote: majority. Appropriation: no. Fiscal committee: no. State-mandated local program: no.

The people of the State of California do enact as follows:

- 1 SECTION 1. Section 53601.7 of the Government Code is
2 amended to read:
3 53601.7. Notwithstanding the investment parameters of
4 Sections 53601 and 53635, a local agency that is a county or a
5 city and county may invest any portion of the funds that it deems
6 wise or expedient, using the following criteria:
7 (a) No investment shall be made in any security, other than a
8 security underlying a repurchase agreement, reverse repurchase
9 agreement, or a securities lending agreement, that, at the time of
10 purchase, has a term remaining to maturity in excess of 397 days,

1 and that would cause the dollar-weighted average maturity of the
2 funds in the investment pool to exceed 90 days.

3 (b) All corporate and depository institution investments shall
4 meet or exceed the following credit rating criteria at time of
5 purchase:

6 (1) Short-term debt shall be rated at least “A-1” by Standard &
7 Poor’s Corporation, “P-1” by Moody’s Investors Service, Inc., or
8 “F-1” by Fitch Ratings. If the issuer of short-term debt has also
9 issued long-term debt, this long-term debt rating shall be rated at
10 least “A,” without regard to +/- or 1, 2, 3 modifiers, by Standard
11 & Poor’s Corporation, Moody’s Investors Service, Inc., or Fitch
12 Ratings.

13 (2) Long-term debt shall be rated at least “A,” without regard
14 to +/- or 1, 2, 3 modifiers, by Standard & Poor’s Corporation,
15 Moody’s Investors Service, Inc., or Fitch Ratings.

16 (c) (1) No more than 5 percent of the total assets of the
17 investments held by a local agency may be invested in the
18 securities of any one issuer, except the obligations of the United
19 States government, United States government agencies, and
20 United States government-sponsored enterprises.

21 (2) No more than 10 percent of the investments held by a local
22 agency may be invested in any one mutual fund.

23 (3) Up to 25 percent of the fair market value of the total assets
24 held by a local agency may be invested in the first tier securities
25 of a single issuer for a period of up to three business days after
26 acquisition. The securities of no more than one issuer may be
27 invested pursuant to this paragraph at a time.

28 (d) Where this section specifies a percentage limitation for a
29 particular category of investment, that percentage is applicable
30 only at the date of purchase. A later increase or decrease in a
31 percentage resulting from a change in values or assets shall not
32 constitute a violation of that restriction. If subsequent to
33 purchase, securities are downgraded below the minimum
34 acceptable rating level, the securities shall be reviewed for
35 possible sale within a reasonable amount of time after the
36 downgrade.

37 (e) Within the limitations set forth in this section, a local
38 agency electing to invest its funds pursuant to this section may
39 invest in the following securities:

1 (1) Direct obligations of the United States Treasury or any
2 other obligation guaranteed as to principal and interest by the
3 United States government.

4 (2) Bonds, notes, debentures, or any other obligations of, or
5 securities issued by, any federal government agency,
6 instrumentality, or government-sponsored enterprise.

7 (3) Registered state warrants or treasury notes or bonds of this
8 state, including bonds payable solely out of the revenues from a
9 revenue-producing property owned, controlled, or operated by
10 the state or by a department, board, agency, or other entity of the
11 state.

12 (4) Bonds, notes, warrants, or other indebtedness of the local
13 agency, or any local agency within this state, including bonds
14 payable solely out of the revenues from a revenue-producing
15 property owned, controlled, or operated by the local agency, or
16 by a department, board, agency, or authority of the local agency.

17 (5) Bankers acceptance, otherwise known as bills of exchange
18 or time drafts drawn on and accepted by a commercial bank,
19 primarily used to finance international trade. Purchases of
20 bankers acceptances may not exceed 180 days to maturity.

21 (6) Short-term unsecured promissory notes issued by
22 corporations for maturities of 270 days or less. Eligible
23 commercial paper is further limited to the following:

24 (A) Issuing corporations that are organized and operating
25 within the United States, having total assets in excess of five
26 hundred million dollars (\$500,000,000).

27 (B) Maturities for eligible commercial paper that may not
28 exceed 270 days and may not represent more than 10 percent of
29 the outstanding paper of an issuing corporation.

30 (7) A certificate representing a deposit of funds at a
31 commercial bank for a specified period of time and for a
32 specified return at maturity. Eligible certificates of deposit shall
33 be issued by a nationally or state-chartered bank or a state or
34 federal association, as defined in Section 5102 of the Financial
35 Code, or by a state-licensed branch of a foreign bank. For
36 purposes of this subdivision, certificates of deposits shall not
37 come within Article 2 (commencing with Section 53630), except
38 that the amount so invested shall be subject to the limitations of
39 Section 53638. The legislative body of a local agency and the
40 treasurer or other official of the local agency having legal

1 custody of the money may not invest local agency funds, or
2 funds in the custody of the local agency, in negotiable certificates
3 of deposit issued by a state or federal credit union if a member of
4 the legislative body of the local agency, or any person with
5 investment decisionmaking authority in the administrative office,
6 manager's office, budget office, auditor-controller's office, or
7 treasurer's office of the local agency also serves on the board of
8 directors, or any committee appointed by the board of directors,
9 other credit committee or the supervisory committee of the state
10 or federal credit union issuing the negotiable certificate of
11 deposit.

12 (8) Repurchase agreements, reverse repurchase agreements, or
13 securities lending agreements of any securities authorized by this
14 section, if the agreements meet the requirements of this
15 paragraph and the delivery requirements specified in Section
16 53601. Investments in repurchase agreements may be made, on
17 any investment authorized by this section, when the term of the
18 agreement does not exceed one year. The market value of the
19 securities that underlay a repurchase agreement shall be valued at
20 102 percent or greater of the funds borrowed against those
21 securities, and the value shall be adjusted no less than quarterly.
22 Because the market value of the underlying securities is subject
23 to daily market fluctuations, the investments in repurchase
24 agreements shall be in compliance with this section if the value
25 of the underlying securities is brought back to 102 percent no
26 later than the next business day. Reverse repurchase agreements
27 may be utilized only when all of the following criteria are met:

28 (A) The security being sold on reverse repurchase agreement
29 or securities lending agreement has been owned and fully paid
30 for by the local agency for a minimum of 30 days prior to the
31 sale.

32 (B) The total of all reverse repurchase agreements on
33 investments owned by the local agency not purchased or
34 committed to purchase does not exceed 20 percent of the market
35 value of the portfolio.

36 (C) The agreement does not exceed a term of 92 days, unless
37 the agreement includes a written codicil guaranteeing a minimum
38 earning or spread for the entire period between the sale of a
39 security using a reverse repurchase agreement and the final
40 maturity date of the same security.

(D) Funds obtained or funds within the pool of an equivalent amount to that obtained from selling a security to a counterparty by way of a reverse repurchase agreement or securities lending agreement, may not be used to purchase another security with a maturity longer than 92 days from the initial settlement date of the reverse repurchase agreement or securities lending agreement, unless the agreement includes a written codicil guaranteeing a minimum earning or spread for the entire period between the sale of a security using a reverse repurchase agreement or securities lending agreement and the final maturity date of the same security.

(E) Investments in reverse repurchase agreements or similar investments in which the local agency sells securities prior to purchase with a simultaneous agreement to repurchase the security, shall only be made with prior approval of the governing body of the local agency and shall only be made with primary dealers of the Federal Reserve Bank of New York or with a nationally or state-chartered bank that has or has had a significant banking relationship with a local agency.

“Securities,” for purposes of this paragraph, means securities of the same issuer, description, issue date, and maturity.

(9) All debt securities issued by a corporation or depository institution with a remaining maturity of not more than 397 days, including securities specified as “medium-term notes,” as well as other debt instruments originally issued with maturities longer than 397 days, but which, at time of purchase, have a final maturity of 397 days or less. Eligible medium-term notes shall be issued by corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States.

(10) (A) Shares of beneficial interest issued by diversified management companies that invest in the securities and obligations described in this subdivision and that comply with the investment restrictions of this section. However, notwithstanding these restrictions, a counterparty to a reverse repurchase agreement shall not be required to be a primary dealer of the Federal Reserve Bank of New York if the company’s board of directors finds that the counterparty presents a minimal risk of default. The value of the securities underlying a repurchase

1 agreement may be 100 percent of the sales price if the securities
2 are marked to market daily.

3 (B) Shares of beneficial interest issued by diversified
4 management companies that are money market funds registered
5 with the Securities and Exchange Commission under the federal
6 Investment Company Act of 1940 (15 U.S.C. Sec. 80a-1 et seq.).

7 (C) All shares of beneficial interest described in this paragraph
8 shall have met either of the following criteria:

9 (i) Attained the highest ranking or the highest letter and
10 numerical rating provided by not less than two nationally
11 recognized statistical rating organizations.

12 (ii) Retained an investment adviser registered or exempt from
13 registration with the Securities and Exchange Commission and
14 who has not less than five years' experience investing in money
15 market instruments and with assets under management in excess
16 of five hundred million dollars (\$500,000,000).

17 (11) Any mortgage passthrough security, collateralized
18 mortgage obligation, mortgage-backed or other paythrough bond,
19 equipment lease-backed certificate, consumer receivable
20 passthrough certificate, or consumer receivable-backed bond.

21 Securities eligible for investment under this paragraph shall be
22 issued by an issuer having an "A" or higher rating from the
23 issuer's debt as provided by a nationally recognized rating
24 service and rated in a rating category of "AA" or its equivalent or
25 better by a nationally recognized rating.

26 (12) Contracts issued by insurance companies that provide the
27 policyholder with the right to receive a fixed or variable rate of
28 interest and the full return of principal at the maturity date.

29 (13) Any investments that would qualify under SEC Rule 2a-7
30 of the Investment Company Act of 1940 guidelines. These
31 investments shall also meet the limitations detailed in this
32 section.

33 (f) For purposes of this section, all of the following definitions
34 shall apply:

35 (1) "Repurchase agreement" means a purchase of securities
36 pursuant to an agreement by which the counterparty seller will
37 repurchase the securities on or before a specified date and for a
38 specified amount and the counterparty will deliver the underlying
39 securities to the local agency by book entry, physical delivery, or
40 by third-party custodial agreement.

1 (2) “Significant banking relationship” means any of the
2 following activities of a bank:

3 (A) Involvement in the creation, sale, purchase, or retirement
4 of a local agency’s ~~bonds~~ *bonds*, warrants, notes, or other
5 evidence of indebtedness.

6 (B) Financing of a local agency’s securities or funds as
7 deposits.

8 (C) Acceptance of a local agency’s securities or funds as
9 deposits.

10 (3) “Reverse repurchase agreement” means a sale of securities
11 by the local agency pursuant to an agreement by which the local
12 agency will repurchase the securities on or before a specified
13 date and includes other comparable agreements.

14 (4) “Securities lending agreement” means an agreement with a
15 local agency that agrees to transfer securities to a borrower who,
16 in turn agrees to provide collateral to the local agency. During
17 the term of the agreement, both the securities and the collateral
18 are held by a third party. At the conclusion of the agreement, the
19 securities are transferred back to the local agency in return for the
20 collateral.

21 (5) “Local agency” means a county or city and county.

22 (g) For purposes of this section, the base value of the local
23 agency’s pool portfolio shall be that dollar amount obtained by
24 totaling all cash balances placed in the pool by all pool
25 participants, excluding any amounts obtained through selling
26 securities by way of reverse repurchase agreements, or other
27 similar borrowing methods.

28 (h) For purposes of this section, the spread is the difference
29 between the cost of funds obtained using the reverse repurchase
30 agreement and the earnings obtained on the reinvestment of the
31 funds.

32 (i) This section shall remain in effect only until January 1,
33 2007, and as of that date is repealed, unless a later enacted
34 statute, that is enacted before January 1, 2007, deletes or extends
35 that date.